

***United States Court of Appeals  
for the Second Circuit***



**BRIEF FOR  
APPELLEE**





ORIGINAL

77-7024

UNITED STATES COURT OF APPEALS  
FOR THE SECOND CIRCUIT

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RICHARD VOIGHT,  
DICK VOIGHT BUICK, INC.;

Plaintiffs-Appellants,

-vs-

Docket No. 77-7024

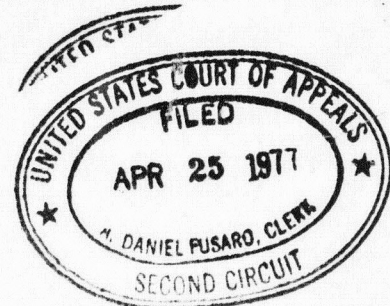
GENERAL MOTORS CORPORATION;  
MOTORS HOLDING DIVISION,  
GENERAL MOTORS CORPORATION;  
BUICK MOTOR DIVISION,  
GENERAL MOTORS CORPORATION;  
GENERAL MOTORS ACCEPTANCE CORPORATION;  
ARGONAUT DIVISION,  
GENERAL MOTORS CORPORATION;  
EDWARD HIGGINS;

Defendants,

and

MARINE MIDLAND BANK,  
HARRY FORNOROLA,  
WILLIAM MONRIAN;

Defendants-Appellees.



---

NATURE OF PROCEEDING : APPEAL

COURT BELOW : UNITED STATES DISTRICT COURT  
WESTERN DISTRICT OF NEW YORK

BRIEF ON BEHALF OF GENERAL MOTORS CORPORATION

PHILLIPS, LYTLE, HITCHCOCK, BLAINE & HUBER  
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BUFFALO, N. Y. 14203

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### STATEMENT

This brief is submitted by General Motors Corporation ("G.M.")<sup>\*</sup> in opposition to plaintiffs' appeal from an order dismissing their complaint as to defendants Marine Midland Bank, Harry Fornorola, and William Monrian. G.M. was not one of the moving parties in respect to the order which plaintiffs appeal -- so that G.M. is not an Appellee. Nevertheless, one of the issues on the appeal -- namely, whether plaintiffs have a claim under the securities laws (specifically, whether a "security" within the meaning of those laws is involved)<sup>\*\*</sup> -- is of interest to G.M. Indeed, this issue is central to plaintiffs' securities law claims against G.M.

### ISSUE PRESENTED

Plaintiffs allege that in 1967 Richard Voight acquired "the franchise of and stock in" an automobile

<sup>\*</sup> General Motors Acceptance Corporation ("G.M.A.C.") and Edward Higgins, an employee of G.M., are also listed as defendants. However, Higgins has not been served, and G.M.A.C. is not concerned with the securities law claims that are the subject of this brief.

<sup>\*\*</sup> The district court's dismissal of plaintiffs' claims under statutes other than the Securities Acts appears to have been based on findings that are not directly relevant to plaintiffs' claims against G.M.



dealership. (Complaint, ¶¶ 112-113.) They further allege:

That the franchise agreements and the stock in the new dealership corporation were and are securities, as defined by the Securities Act of 1933, and the Securities Exchange Act of 1934, and are subject to regulation thereunder. (Complaint, ¶ 114.)

The issue is whether the franchise agreement or stock was a "security" within the meaning of the Securities Acts.

#### STATUTES INVOLVED

Section 2(1) of the Securities Act, 15 U.S.C.A.

§ 77(b) provides as follows:

The term "security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

For purposes of this appeal, there are no significant differences between the above definition and that contained in § 3(a)(10) of the Securities Exchange Act, 15 U.S.C.A. § 78(c)(10).



ARGUMENT

POINT ONE

PLAINTIFFS DID NOT OWN A "SECURITY" WITHIN  
THE MEANING OF THE SECURITIES ACTS.

The fact that the complaint refers to "stock"  
as well as "franchise agreements" does not alter the  
principles that control this case.

As observed by the United States Supreme Court  
in United Housing Foundation, Inc. v. Forman, 421 U.S.  
837, 849 (1975):

Because securities transactions are economic  
in character Congress intended the application  
of these statutes to turn on the economic  
realities underlying a transaction, and not on  
the name appended thereto.

" . . . [S]imply because the statutory definition of a  
security includes the words 'any . . . stock'" does not  
mean that every transaction evidenced by the sale of  
shares called "stock" is a security transaction. 421  
U.S. at 848.

As this Court observed in the same case:

To look to the substance of the term "stock"  
is in essence to determine if an "investment  
contract" of some sort exists. The basic test  
to ascertain the presence of an "investment  
contract" was formulated by the Supreme Court  
in SEC v. W. J. Howey Co. . . . .

Forman v. Community Services, Inc., 500 F.2d 1246, 1253,  
(2d Cir. 1974) rev'd. on other grounds sub nom. United  
Housing Foundation, Inc. v. Forman, supra.

Applying the Howey test to the facts of this case demonstrates that neither the "stock" nor "franchise agreements" -- whether considered separately or together -- meets the statutory definition of a "security." Howey defines an "investment contract" as "[1] an investment of money [2] in a common enterprise [3] with profits to come solely from the efforts of others." SEC v. W. J. Howey Co., 328 U.S. 293, 301 (1946).

It is plain from the allegations of the complaint that plaintiffs' interests (either the stock, franchise, or both) do not satisfy the Howey test; they were not the interests of a passive investor in another's enterprise. Profits would derive substantially from Richard Voight's own efforts; certainly not "solely from the efforts of others." Under such circumstances, courts have consistently held that the interests are not "securities."

For example, in Mr. Steak, Inc. v. River City Steak, Inc., 460 F.2d 666 (10th Cir. 1972) the Tenth Circuit held that a franchise to operate a restaurant was not a "security." The court explained that an investment interest is a "security" where it is purchased by a wholly passive investor who lacks the skill and knowledge to conduct the business himself:



"Here, in contrast, it does not appear that River City Steak was an uninformed investor. It was acquainted with the nature of the business it undertook. Even though a 'turn-key' operation was sold, it remained the sale of a business which the defendant could control and included the normal risks incident to operation of any enterprise. See *Chapman v. Rudd Paint & Varnish Co.*, 409 F.2d 635 (9th Cir. 1969), where a similar 'turn-key' distributorship was held not to involve the sale of securities . . . .

"Additionally, defendant has not endeavored to show that it was prevented from directing the operations of the restaurant or that it lacked the requisite knowledge, skill or expertise to undertake that task. Defendant here bought the 'chance to make a great deal of money,' but only if it could successfully operate the restaurant. *Roe v. United States*, 287 F.2d 435, 439 (5th Cir. 1961); *Continental Marketing Corp. v. S. E. C.*, [387 F.2d 466 (10th Cir. 1967)], citing *Roe*. We contrast the usual investor-promoter situation, where the skill or ingenuity of the investor does not determine the success or failure of the venture and where the investor's fortunes parallel those of the promoter, to the present situation, where River City Steak's enterprise stands or falls independently of Mr. Steak's success or failure. See, e.g., *S. E. C. v. W. J. Howey Co.*, supra; *Continental Marketing Corp. v. S. E. C.*, supra; *Farrell v. United States*, 321 F.2d 409 (9th Cir. 1963); *Roe v. United States*, supra; *Blackwell v. Bentsen*, 203 F.2d 690 (5th Cir. 1953); *Penfield Co. of California*, 143 F.2d 746 (9th Cir. 1944); *S. E. C. v. Universal Service Ass'n*, 106 F.2d 232 (7th Cir. 1939); *S. E. C. v. MacElvain*, 299 F. Supp. 1352 (M.D. Ala. 1969). To characterize the contracts which create this relationship as a security would work an unwarranted extension of the Securities Act of 1933."

460 F.2d at 670, quoting Mr. Steak, Inc. v. River City Steak, Inc., 324 F. Supp. 640, 645-46 (D. Colo. 1970).



Similarly, in Beefy Trail, Inc. v. Beefy King International, Inc., 348 F. Supp. 799 (M.D. Fla. 1972), the court held that a restaurant franchise was not a "security," where it was evident to the court that the franchisee

"wasn't interested in speculation." He had previously helped other franchisees set up their own operations and he felt he could do so without too much trouble. He was primarily interested in buying a business, setting it up and operating it.

The deposition reveals that he was a businessman, interested in operating his own business, who had extensive prior business experience which he contemplated bringing to the beef sandwich business, and that he actively participated in the daily operation of the franchise, overseeing the restaurant's regular operations, its advertising, kept the books and records, and regularly made business decisions affecting the restaurant.

348 F. Supp. at 805.

The complaint itself reveals that, like the franchisees in the cases discussed above, Voight was not interested in investing in a common enterprise that was managed, controlled, and operated by persons other than himself. Rather, he was interested in doing what he had done before, namely, operating a business:

[P]rior to Plaintiff RICHARD VOIGHT'S moving to Rochester, New York, Plaintiff had been employed in various aspects of the automobile retail business in and around Chicago, Illinois, and had been recognized by GENERAL MOTORS CORPORATION and others for his outstanding performance in selling of Buick



automobiles, parts and accessories, as well as in operating, running and managing an automobile dealership.

(Complaint, ¶ 4) (Emphasis supplied).

It is alleged that the significant efforts that determined the fortunes of Voight's investment were his own; i.e., his efforts, and not those of others, were the primary source of the profits of the franchise:

Plaintiff, RICHARD VOIGHT, ran, operated and managed DICK VOIGHT BUICK, INC., successfully generated profits and was recognized by Defendant, GENERAL MOTORS CORPORATION and its BUICK MOTOR DIVISION, and others, for his achievements and success.

(Complaint, ¶ 5) (Emphasis supplied.) Thus, plaintiffs themselves have demonstrated in the complaint that their interests lacked the traditional attributes that make an investment a "security".

In his appeal brief to this Court (p. 24), counsel for Voight refers to the more expansive test of a "security" adopted by the Ninth Circuit in SEC v. Glenn W. Turner Enterprises, Inc., 474 F.2d 476 (9th Cir. 1973), cert. denied, 414 U.S. 821 (1973). Under this test, an investment is a "security" where "the efforts made by those other than the investor are the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise." 474 F.2d at 482. •

As the language quoted above indicates, even under the Glenn Turner analysis, significant participation by a franchisee in his business will negate a finding that the franchisee's interest is a "security." As one court has stated, the Glenn Turner analysis brings within the scope of the Securities Acts only those franchise agreements "which give the franchisee no meaningful control over his own enterprise." Wieboldt v. Metz, 355 F. Supp. 255, 260 (S.D.N.Y. 1973). Indeed, in Bitter v. Hoby's International, Inc., 498 F.2d 183 (9th Cir. 1974), the Ninth Circuit, the author of Glenn Turner, itself held that a typical restaurant franchise was not a "security":

the focus here must be on the extent of participation the franchisee has under the franchise agreement. In Turner, the purported success of the investment depended primarily upon the selling efforts of the [franchisor's] employees and distributors, and not on the slight efforts of the investors. By contrast the efforts required of the Hoby's franchisee were qualitatively more substantial, entailing continuous operation of the restaurant, production and sale of roast beef sandwiches and related products, purchase of materials, merchandise and supplies from sources selected at his sole discretion, preparation of monthly operating statements, and employment of personnel to accomplish the foregoing.

The contractual restrictions on the discretion of the franchisee were designed merely to effectuate the purported benefits of standardization derived from participation in a restaurant chain. They did not render the franchisee's efforts minimal. In spite



of regulation, each franchisee's active management was essential to the success of his retail restaurant.

498 F.2d at 184-85 (Citations omitted).

As discussed above, the complaint shows that Voight's efforts were the significant ones in the success or failure of the dealership. Even under the more expansive Glenn Turner test, Voight's investment lacked the essential attributes of a "security." The dominant "economic reality" of Voight's transaction was to enable him to operate, manage, and direct a Buick dealership. There is neither authority nor logical argument for the proposition that such a transaction should fall within the scope of the Securities Acts.

POINT TWO

THE VOIGHT COMPLAINT CONTAINS NO ALLEGATIONS THAT MIGHT REQUIRE A FULLER CONSIDERATION OF THE NATURE OF THE FRANCHISE INTEREST.

In his brief, counsel for plaintiffs states that there exists a question of fact whether the franchise agreement constituted "security." He argues that the district court should not have ruled as it did without more fully scrutinizing "the relation of power between franchisor and franchisee" (p. 26). Elsewhere (p. 21) he suggests that the district court should have examined more fully the features possessed by his stock in the dealership.

This argument is rebutted by the "economic reality" of the investment as that is alleged in the complaint. As discussed in Point One, supra, the complaint demonstrates that Voight's purpose was not to engage in passive investment, but to become operating head of a dealership holding a Buick franchise. Furthermore, counsel gives no indication how, if given the opportunity, he would attempt to prove that the "economic reality" of the investment was the purchase of a "security." The comments of the Third Circuit in a similar case are here instructive:

In his brief, [plaintiff] contends that he "alleges factual contentions which call



into question the meaning and substance of the [franchise] agreement." If this were so, we might well agree with [plaintiff] that the district court should not have determined whether the agreements were securities without a fuller factual exposition. It would seem that only through examining all the facts and circumstances surrounding the agreement could the Supreme Court's mandate to emphasize economic reality be given full effect. But we must agree with the conclusion of the district court that nowhere does [plaintiff] allege that the arrangements involved anything other than what was stated in the documents.

Lino v. City Investing Co., 487 F.2d 689, 693 (3rd Cir. 1973).

CONCLUSION

The judgment of the district court dismissing plaintiffs' claims of violations of the Securities Acts should be affirmed.

Dated: Buffalo, New York  
April 11, 1977

Respectfully submitted,

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STATE OF NEW YORK     )  
                              ) SS.:  
COUNTY OF ERIE         )

PAUL K. STECKER, being duly sworn, deposes and says that he is not a party to this action, that he is over 18 years of age, that he resides in Buffalo, New York; and

That on April 11, 1977, deponent served the annexed Brief on the following:

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by depositing a copy of same, enclosed in a postpaid properly addressed wrapper, in an official depository under the exclusive care and custody of the United States Postal Service.

Paul K. Stecker

Sworn to before me this  
11th day of April, 1977.

Anne M. Williams  
Notary Public

**ANNE M. WILLIAMS**  
Notary Public, State of New York  
Qualified in Erie County  
My Commission Expires March 30, 1978